



Raytheon Financial Analysis

Project 1
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Headquartered in Waltham, Mass., Raytheon Company (NYSE: RTN) is an American defense contractor specializing in defense, civil government and cybersecurity¹. Raytheon is one of the United States government's top defense contractors, working with the US Department of Defense, US Armed Forces, US Intelligence Community, FAA, NOAA, NASA and others². Based on analysis of quarter two data from 2014 to 2016 used to create a pro-forma analysis, Raytheon can expect total sales of \$12.2 billion by the end of the second quarter of 2017, a net income of \$1.07 billion and an estimated earnings-per-share of 3.60 (Table 1).

Raytheon is within the "Industrial Goods" sector and the "Aerospace/Defense Products & Services" industry². Its primary competitors are other US defense contractors, including Northrop Grumman, Lockheed Martin, General Dynamics and L-3 Communications³.

For this analysis, I selected Lockheed Martin (LMT) and Northrop Grumman (NOC) as my comparison companies. Lockheed Martin is the largest of Raytheon's direct competitors with the highest current stock value and revenue (\$46 billion in 2015)³; and Northrop Grumman and Raytheon had similar total 2015 revenue of around \$23 billion⁴.

Short-term Solvency (Table 3): Raytheon's current ratio sat at 1.64 and its acid ratio sat at 1.53 in Q2 2016, which indicates high financial stability, and its short-term solvency ratios have gone up since Q2 2015 and Q1 2016 (the ratio was at its highest in 2014, when Raytheon had approximately \$1 billion more cash on-hand than in later reviewed quarters) (Table 1).

Raytheon's short-term solvency is higher than both NOC and LMT because it retains more cash-on-hand and lower inventory levels than its competitors.

Long-term Solvency (Table 3): Raytheon's total debt ratio was 0.183, which is right about where a company should be when considering long-term solvency. However, Raytheon does not report short-term debt on its financial statements (Table 1), so that number could be artificially deflated. Comparing the total debt ratio to those of both NOC (0.265) and LMT (0.294), the number appears to be fairly consistent within the industry.

Raytheon's debt-equity ratio is 0.517, which is significantly lower than the ratios of NOC (1.124) and LMT (4.941). Again, this number may be artificially deflated because of the lack of short-term debt being reported (Table 1), but will still remain much lower. A high debt-equity ratio

¹ Investor Relations Factsheet, Raytheon.com

² Raytheon Company, Yahoo! Finance.

³ Lockheed Martin Corporation, Yahoo! Finance.

⁴ Northrup Grumman, Yahoo! Finance.

indicates a company is taking on more risk with its investment. Raytheon, LMT and NOC have all received major contracts with US defense agencies, so those higher debt-equity ratios may be a result of those contracts.

Asset Management (Table 3): When looking at asset management for companies like Raytheon and its competitors that operate primarily with major contracts on high-cost products, AP and AR turnover is less important, so total asset turnover is one of the only real measures. Raytheon's Total asset turnover has been around 0.40 at Q2 end for the last three years, which is lower than both NOC (0.496) and LMT (0.488). One major reason for the difference is that Raytheon keeps nearly \$1 billion more cash on hand than both LMT and NOC (Table 1).

Profitability (Table 1): At 74.4% of sales, Raytheon's COGS is relatively lower than the COGS of both LMT (89.2%) and NOC (76.5%), giving it a higher gross margin and profit margin (Tables 1 and 3). Raytheon has significantly more retained earnings (59.2% of total assets) than both NOC (44.2%) and LMT (27.4%), meaning its ROE is lower (11%) than NOC and LMT (18.9% and 64%, respectively). The ROE of 11% is bad for investors because it indicates that Raytheon is less efficient at using investment than NOC and LMT (a ROE of 64% is a good sign).

Pro Forma (Tables 1 and 2): Raytheon predicts a year-end 2016 revenue of \$24-24.5 billion (Table 2), or an increase in gross revenue of 4%. Based on past years' increases and recent major contracts, I feel that this prediction is fair.

COGS and SGA proportions, effective tax rate and long-term debt will be similar to those in years past. Based on growth from previous years, retained net income will increase by another 5% from 2016, and inventory will increase by 25%. PPE will grow at 5% (Table 2). The projected earnings per share will be 3.60 (Table 1).

Although sales are projected to increase over 2016, COGS and SG&A expenses are also expected to rise, causing the projected earnings per share (3.60, Table 1) to be slightly lower than that in 2016.

Conclusion: Overall, Raytheon will continue to see growth within its industry, and a comparison to competitors in the industry, Raytheon operates efficiently in many aspects (notably COGS and, by extension, gross margin and net income, and current assets. (Tables 1 and 2).

Table 1

Income Statements and Balance Sheets

	RTN					LMT		NOC
	Q2 2017	Q2 2016	Q1 2016	2015	2014	Q2 2016	Q2 2016	
		7/3/2016	4/3/2016	6/28/2015	6/29/2014	6/26/2016	6/30/2016	
INCOME STATEMENT								
(in millions)								
Revenue:								
Sales	12,270	11,798	5,763	11,136	11,209	24,616	11,956	
COGS	9,202	8,780	4,400	8,358	8,462	21,957	9,144	
SG&A Expenses	1,534	1,446	751	1,290	1,200	(204)	1,276	
Operating Income:	1,534	1,572	612	1,488	1,547	2,863	1,536	
Other Income/Expenses Net	(10)	(11)	(6)	(9)	(11)	1	20	
EBIT:	1,544	1,583	618	1,497	1,558	2,864	1,556	
Interest Expense	110	116	58	117	105	330	150	
EBT:	1,434	1,467	560	1,380	1,453	2,534	1,406	
Taxes	401	358	156	324	359	615	333	
Net Income (Continued Ops):	1,032	1,109	404	1,056	1,094	1,919	1,073	
Discontinued Operations:	-	-	1	1	59	-	-	
Net Income from noncontrolling interests	(34)	(29)	(24)	1	6	-	-	
Net Income (Total):	1,066	1,138	429	1,056	1,147	1,919	1,073	

Table 1, ctd.

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BALANCE SHEET								
(in millions)								
Assets								
Cash	2,459	2,016	1,934	1,828	3,261	1,269	1,139	
Short-term Investments	750	703	711	666	915	-	-	
Inventory	839	671	637	519	430	5,136	973	
Other Current Assets	6,783	6,460	6,077	5,691	5,693	9,668	3,669	
Total Current Assets:	10,831	9,850	9,359	8,704	10,299	16,073	5,781	
Property, Plant & Equipment	2,129	2,028	2,018	1,929	1,878	5,438	3,299	
Goodwill	14,901	14,791	14,791	14,683	12,765	13,621	12,463	
Other Long-term Assets	1,969	2,429	2,661	3,121	1,438	15,276	2,538	
Total Assets:	29,830	29,098	28,829	28,437	26,380	50,408	24,081	
Liabilities & Shareholder Equity								
Accounts Payable	4,600	4,654	4,243	4,213	4,597	12,026	3,767	
Short-term Debt	-	-	-	-	-	502	-	
Other Short-term Liabilities	1,360	1,360	1,506	1,428	1,299	3,067	1,332	
Total Current Liabilities:	5,960	6,014	5,749	5,641	5,896	15,595	5,099	
Long-term Debt	5,333	5,333	5,332	5,333	4,736	14,307	6,387	
Other Long-term Liabilities	7,100	7,092	7,108	6,865	3,854	17,509	6,914	
Total Liabilities:	18,393	18,439	18,189	17,839	14,486	47,411	18,400	
Minority Interest	500	343	516	542	166	-	-	
Additional Paid-in Capital	-	-	30	834	1,566	-	-	
Common Stock	3	3	3	3	3	301	179	
Retained Earnings	17,934	17,212	17,141	16,314	14,945	13,800	10,634	
Surplus	-	-	-	-	-	-	-	
Treasury Stock	-	-	-	-	-	-	-	
Other Stockholder Equity	(7,000)	(6,899)	(7,050)	(7,095)	(4,786)	(11,104)	(5,132)	
Total Equity:	10,937	10,316	10,124	10,056	11,728	2,997	5,681	
Total Liabilities & Equity:	29,830	29,098	28,829	28,437	26,380	50,408	24,081	
Shares Outstanding - Basic	296	298.2	299.2	306.8	313.9	303.8	182.4	
Earnings Per Share	3.60	3.82	1.43	3.44	3.65	6.32	5.88	

Table 2

*Pro Forma Assumptions***Raytheon's Financial Outlook for year-end 2016**

Net Sales	24,250
Deferred Rev Adjustment	(77)
Amortization	(121)
FAS/CAS Adjustment	428
Interest expense	(220)
Effective Tax Rate	28%
Diluted Shares (Million)	297
EPS from Cont.	7.23
Operating Cash Flow	2,950

My Assumptions:

Revenue	+ 4%
Depreciation	265
Interest	(110)
Effective Tax Rate	28%
COGS (percent of sales)	75%
SGA (percent of sales)	12.5%
Amt of Net Income Retained (120% of 2014 value)	17,934
Diluted Shares (Million)	296
Inventory	+ 25%
PPE	+ 5%
Other Current Assets	+ 5%
Short-term Investments	+ \$50M
Other Stockholder Equity same as last year	
Short-term Liabilities will remain the same	
Accounts Payable will remain the same	
Discontinued operations remain the same	
Long Term Debt and Liabilities remain the same	
Minority Interest same as last year	
Cash will be the plug value	

Table 3
Financial Ratio Calculations

		RTN				LMT	NOC
		Q2 2016	Q1 2016	Q2 2015	Q2 2014	Q2 2016	Q2 2016
Short Term Solvency (Liquidity)							
Current Ratio	Current Assets/ Current Liabilities	1.638	1.628	1.543	1.747	1.031	1.134
Quick (Acid) Ratio	(Current Assets-Inventory)/Current Liabilities	1.526	1.517	1.451	1.674	0.701	0.943
Interval Measure (days)	Current Assets/(CoGS/365)	204.741	194.093	190.055	222.119	133.594	115.380
Long Term Solvency							
Total Debt Ratio	Total Debt/Total Assets	0.183	0.185	0.188	0.180	0.294	0.265
Debt-Equity Ratio	Total Debt/Total Equity	0.517	0.527	0.530	0.404	4.941	1.124
Cash Coverage Ratio	(EBIT + Depreciation)/Interest Expense	15.776	12.793	14.701	16.895	10.476	11.767
Profitability							
GM %	Gross Margin/Revenue	25.6%	23.7%	24.9%	24.5%	10.8%	23.5%
Profit Margin	Net Income/Sales	0.096	0.074	0.095	0.102	0.078	0.090
ROA	Net Income/Assets	0.039	0.015	0.037	0.043	0.038	0.045
ROE	Net Income/Equity	0.110	0.042	0.105	0.098	0.640	0.189
ROE (DuPont Identity)	(Net Income/Sales)(Sales/Assets)(Assets/Equity)	0.110	0.042	0.105	0.098	0.640	0.189
Asset Management							
AR Turnover	Sales/AR					2.654	3.433
Days Sales in AR (days)	365/(Sales/AR)					68.764	53.166
Inventory Turnover	CoGS/Inventory	13.085	6.907	16.104	19.679	4.275	9.398
Days Sales in Inventory (days)	365/(CoGS/Inventory)	13.947	13.211	11.333	9.274	42.689	19.420
AP Turnover	CoGS/AP	1.887	1.037	1.984	1.841	1.826	2.427
Days Sales in AP (days)	365/(CoGS/AP)	96.737	87.994	91.992	99.144	99.957	75.183
Total Asset Turnover	Total Sales/Total Assets	0.405	0.200	0.392	0.425	0.488	0.496
Market Value Ratios							
Earnings Per Share - Basic (EPS)	Net Income/Shares Outstanding	3.82	1.43	3.44	3.65	6.32	5.88
Price-Earnings Ratio (PE)	Market Price/EPS	35.737	-	-	-	37.531	35.433
Market-to-Book Ratio	(Shares Outstanding*Market Price)/Book Equity	3.942	-	-	-	24.031	6.692
Taxes							
Effective Tax Rate	Taxes Paid/EBT	24.4%	27.9%	23.5%	24.7%	24.3%	23.7%

Sources for Financial Statements:

Raytheon Q2 2016: <http://raytheon.mediaroom.com/2016-07-28-Raytheon-Reports-Strong-Second-Quarter-2016-Results>

Raytheon Q1 2016: <http://raytheon.mediaroom.com/2016-04-28-Raytheon-Reports-Solid-First-Quarter-2016-Results>

Raytheon Q2 2015: <http://raytheon.mediaroom.com/2015-07-23-Raytheon-Reports-Solid-Second-Quarter-2015-Results>

Raytheon Q2 2014: <http://raytheon.mediaroom.com/index.php?s=43&item=2617>

Lockheed Martin Q2 2016 (PDF):

<http://www.lockheedmartin.com/content/dam/lockheed/data/corporate/documents/earnings/2016/q2-16-earnings-attachments.pdf>

Northrup Grumman Q2 2016:

<http://investor.northropgrumman.com/phoenix.zhtml?c=112386&p=irol-irhome>

Other financial information, including current stock price, taken from Yahoo! Finance.

Current stock price obtained on September 14, 2016, at 3:15 p.m. EST.